



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

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Contact Person:

ID Number:

Telephone Number:

Taxpayer Identification Number:

SE:T:EO:RA:T:2

A =

B =

X =

Y =

Dear :

This is in response to a letter from your authorized representative dated August 3, 2006, requesting a ruling on your behalf regarding the tax consequences associated with the transactions described below.

Facts:

A is a publicly supported charity exempt from Federal income taxation under Section 501(c)(3) of the Internal Revenue Code (Code) and classified as other than a private foundation under Sections 509(a)(1) and 170(b)(1)(A)(vi) of the Code. In furtherance of its charitable purposes, A promotes economic and environmentally sensitive development in low-income and economically depressed communities. A furthers its exempt purposes by making loans to individuals, non-profit organizations, entrepreneurs and local jurisdictions who are unable to access capital from conventional sources or markets in order to accomplish economic, social and civic development objectives

A was formed under the laws of State X and is registered to do business in State Y.

B is a publicly supported charity exempt from taxation under Section 501(c)(3) of the Code and is classified as other than a private foundation since it is described in Section 509(a)(2) of the Code. B is a community development financial institution that provides loans and technical assistance to small businesses and nonprofit organizations that are unable to access support from traditional sources such as banks. B conducts its activities in States X and Y.

A and B are very similar in terms of charitable purpose, activities, assets and liabilities. Due to these similarities, A and B represent that by combining their respective resources, they will be better able to provide services to meet their exempt purposes. Pursuant to the Agreement and Plan of Merger that is the subject of this ruling request (the "Merger Agreement"), the parties will

execute and file with the Secretary of State of X, Articles of Merger and the Plan of Merger. On the effective date as provided in such filing, B will merge with and into A in a statutory merger under State X law, with A being the surviving entity in the merger.

The merger will result in the transfer by operation of law to A of all assets and liabilities held by B as of the effective date of such merger. B and A represent that all of the assets being transferred from B to A are used in furtherance of and are substantially related to B's exempt purposes and will be used by A in furtherance of and will be substantially related to its exempt purposes.

You have requested the following rulings in connection with the proposed merger transaction:

1. The merger will not result in the revocation of or otherwise adversely affect A's continued tax-exempt status and non-private foundation status under Sections 501(c)(3), 509(a)(1) and 170(b)(1)(A)(vi) of the Code.
2. Any transfers of funds, assets, liabilities and/or personnel in connection with the merger from B to A will not generate unrelated business taxable income to A or to B under Sections 511 through 514 of the Code.
3. The contemplated transfer of assets and liabilities from B to A to effectuate the merger will be considered an "unusual grant" pursuant to Section 1.170A-9(e)(6)(ii) and (iii) of the Income Tax Regulations ("Regulations"), and A can exclude that transfer from both the numerator and the denominator of the support test described in section 170(b)(1)(A)(vi) of the Code.

Law:

Section 501(a) of the Code provides an exemption from federal income tax for organizations described in Section 501(c)(3), including organizations that are organized and operated exclusively for charitable, educational or scientific purposes.

Section 1.501(c)(3)-1(d)(2) of the Regulations provides that the term "charitable" is used in Section 501(c)(3) of the Code in its generally accepted legal sense. The term "charitable" includes the promotion of social welfare by organizations designed to relieve the poor and distressed or the underprivileged, to lessen neighborhood tensions, to eliminate prejudice and discrimination, or to combat community deterioration.

Section 509(a)(1) of the Code provides that a Section 501(c)(3) organization is other than a private foundation if it is described in Section 170(b)(1)(A) (other than in clauses (vii) and (viii)). An organization described in Section 170(b)(1)(A)(vi) of the Code is one which is referred to in Section 170(c)(2) and which normally receives a substantial part of its support (exclusive of income received in the exercise or performance of its charitable, educational, or other purpose or function constituting the 170(c)(1) of the Code or from direct or indirect contributions from the basis for its exempt status) from a governmental unit referred to in Section 170(c)(1) or from direct or indirect contributions from the general public.

Section 1.170A-9(e)(2) of the Regulations states that an organization will be treated as "publicly supported" for purposes of Section 170(b)(1)(A)(vi) of the Code if it normally receives at least

33-1/3 percent of its total support from governmental units or from contributions made directly or indirectly by the general public.

Section 1.170A-9(e)(3) of the Regulations describes the facts and circumstances test under which an organization which does not meet the 33-1/3 percent test may still be considered publicly supported. Generally, that Section provides that an organization must receive at least 10 percent of its total support from governmental units, from contributions made directly or indirectly by the general public, or from a combination of these sources; must be organized and operated so as to attract new and additional public or governmental support on a continuous basis; and, must have a governing body which represents the broad interest of the public, rather than the personal or private interests of a limited number of donors.

Section 509(a)(2) of the Code provides that a Section 501(c)(3) organization is other than a private foundation if it (A) normally receives more than one-third of its support in each taxable year from any combination of (1) gifts, grants, contributions, or membership fees, and (2) gross receipts from admissions, sales of merchandise, performance of services, or furnishing of facilities, in an activity which is not an unrelated trade or business, excluding receipts from any person or from a governmental agency which exceed the greater of \$5,000 or 1 percent of the organization's support in such taxable year, and (B) normally receives not more than one-third of its support in each taxable year from the combined sum of gross investment income and the excess (if any) of the amount of the unrelated business taxable income (as defined in Section 512 of the Code) over the amount of the tax imposed by Section 511 of the Code.

Section 511(a) of the Code imposes a tax on the unrelated business income of organizations described in Section 501(c).

Section 512(a)(1) of the Code defines unrelated business taxable income as the gross income derived by an organization from any unrelated trade or business regularly carried on by it, less the allowable deductions which are directly connected with the carrying on of the trade or business, with certain modifications. Section 512(b)(1) of the Code provides, in part, that interest and dividends are excluded from the computation of an exempt organization's unrelated business taxable income.

Section 513(a) of the Code defines unrelated trade or business as any trade or business the conduct of which is not substantially related (aside from the need of the organization for funds or the use it makes of the profits derived) to the exercise of the organization's exempt purposes or functions.

Section 1.513-1(d)(2) of the Regulations provides, in part, that a trade or business is related to exempt purposes only where the conduct of the business activities has a causal relationship to the achievement of exempt purposes; and it is substantially related for purposes of Section 513 of the Code only if the causal relationship is a substantial one. Thus, for the conduct of trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of exempt purposes.

Section 514(a) of the Code defines the term "unrelated business taxable income" to include a percentage of the net income derived from "debt-financed property." This percentage, in general, has as its numerator and denominator the average "acquisition indebtedness" and the average adjusted basis, respectively, for the year with respect to the debt-financed property.

Section 514(b)(1)(A) of the Code defines the term "debt-financed property" to mean property that is held to produce income and with respect to which there is an "acquisition indebtedness," not including any property substantially all the use of which is substantially related (aside from the need of the organization for income or funds) to the exercise or performance by such organization of its charitable, educational, or other exempt purposes.

Section 1.170A-9(e) of the Regulations generally provides that an organization qualifies as a Section 170(b)(1)(A)(vi) non-private foundation if it is described in Section 170(c)(2) of the Code and is publicly supported (by normally receiving at least one-third of its total support from governmental units or contributions from the general public, or at least ten percent in certain situations).

Section 1.170A-9(e)(6)(i) of the Regulations generally provides that contributions by any corporation shall be taken into account as support from direct or indirect contributions from the general public only to the extent that the total amount of the contributions from such corporation during the relevant period does not exceed 2% of the organization's total support for the period. The 2% limitation generally does not apply to contributions from Section 170(b)(1)(A)(vi) organizations.

Section 1.170A-9(e)(6)(ii) of the Regulations provides that certain contributions may be excluded as unusual grants in determining public support. The exclusion is generally intended to apply to substantial contributions from disinterested parties which: (a) are attracted by reason of the publicly supported nature of the organization; (b) are unusual or unexpected in amount; and (c) would, by reason of their size, adversely affect the status of the organization as normally being publicly supported for the applicable period.

Section 1.170A-9(e)(6)(iii) of the Regulations provides that all pertinent facts and circumstances will be taken into account in determining whether a particular contribution is an unusual grant. No single factor will necessarily be determinative.

Section 1.170A-9(e)(7)(i) of the Regulations generally provides that for purposes of Section 170(b)(1)(A)(vi) of the Code, the term support does not include: (a) any amounts received from the exercise or performance by an organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under Section 501(a) of the Code, or (b) contributions of services for which a deduction is not allowable.

#### First Ruling Request

Your first requested ruling is that the merger will not result in the revocation of or otherwise adversely affect A's continued tax-exempt status and non-private foundation status under Sections 501(c)(3), 509(a)(1) and 170(b)(1)(A)(vi) of the Code.

A's pre-merger activities meet the definition of "charitable" provided in Regulation Section 1.501(c)(3)-1(d)(2). A will not adversely affect its tax exempt status under Section 501(c)(3) of the Code by the proposed merger transaction because it will continue to engage in substantially similar activities which will continue to be "charitable" activities within the meaning of Section 1.501(c)(3)-1(d)(2) of the Regulations following such merger. For identical reasons, A also will continue to qualify as a non-private foundation under Section 509(a)(1) of the Code. Until the time of the proposed merger, B and A will continue to operate and receive financial support in substantially the same manner which provided the basis for determining their respective tax-exempt classifications. Based on the sources of support for A and B, A will continue to qualify for non-private foundation status under Section 509(a)(1) of the Code following completion of the merger.

#### Second Ruling Request

Your second requested ruling is that any transfers of funds, assets, liabilities and/or personnel in connection with the merger from B to A will not generate unrelated business taxable income to A or to B under Sections 511 through 514 of the Code.

Contributions to organizations exempt from federal income tax under Section 501(c)(3) of the Code do not fall within the definition of unrelated business income under Section 512 of the Code, nor do they create taxable gain or loss to the transferor or transferee. Moreover, all assets to be transferred from B to A in the merger shall be utilized in the furtherance of A's exempt purposes, and thus have a substantial causal relationship with such purposes. The tax on unrelated business income is not applicable to this transaction because the Code and Regulations exclude from the definition of unrelated trade or business any trade or business that contributes importantly to the accomplishment of an organization's exempt purposes. Moreover, A will obtain no "debt-financed property" as a result of the merger, since B does not currently own, and will not be transferring to A, any property that is subject to acquisition debt and is used in a manner that is not substantially related (aside from the need of the organization for income or funds) to the exercise or performance of B's, and later A's, exempt purposes.

#### Third Ruling Request

Your third requested ruling is that the contemplated transfer of assets and liabilities from B to A to effectuate the merger will be considered an "unusual grant" pursuant to Section 1.170A-9(e)(6)(ii) and (iii) of the Regulations, and A can exclude that transfer from both the numerator and the denominator of the support test described in Section 170(b)(1)(A)(vi) of the Code.

Based on the facts of this case, including the fact that the transfer of B's assets and liabilities to A is a one-time event necessitated by the merger, the transfer qualifies as an unusual grant as described in Section 1.170A-9(e)(6)(ii) and (iii) of the Regulations.

Accordingly, based on all the facts and circumstances described above, we rule as follows:

1. The merger will not result in the revocation of or otherwise adversely affect A's continued tax-exempt status as a non-private foundation under Sections 501(c)(3) and 509(a)(1) of the Code.
2. Any transfers of funds, assets, services and/or personnel in connection with the merger from B to A will not generate unrelated business taxable income to A or B under Sections 511 through 514 of the Code.
3. The contemplated transfer of funds, assets, services and/or personnel and liabilities from B to A to effectuate the merger is an "unusual grant" pursuant to Section 1.170A-9(e)(6)(ii) and (iii) of the Regulations, and A can exclude that transfer from both the numerator and the denominator of the support test described in Section 170(b)(1)(A)(vi) of the Code.

These rulings are based on the understanding that there will be no material changes in the facts upon which they are based.

These rulings are directed only to the organization that requested them. Section 6110(k)(3) of the Code provides that they may not be used or cited by others as precedent.

This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections cited. We are not ruling that the organizations' economic development activities are conducted in a charitable manner and accomplish charitable purposes, but accept the taxpayer's representation in this regard for purposes of the ruling.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, Notice of Intention to Disclose. A copy of this ruling with deletions that we intend to make available for public inspection is attached as Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown on the heading of this letter.

In accordance with the Powers of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

Robert C. Harper, Jr.  
Manager, Exempt Organizations  
Technical Group 2